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UNCLAS SECTION 01 OF 02 MAPUTO 000653

SIPDIS
SENSITIVE
STATE FOR AF/S - TREGER
DAKAR FOR FAA REP ED JONES
E.O. 12958: N/A
TAGS: EAIR ETRD MZ
SUBJECT: MOZAMBIQUE - RIVAL AIRLINES VIE FOR DOMESTIC MARKET

REF: 04 MAPUTO 1658

¶1. (SBU) Summary. The ongoing fare war between government-owned Linhas Aereas de Mocambique (LAM) and upstart private airline Air Corridor has quickly turned Mozambique from one of the most expensive places in Africa for domestic flights to one of the cheapest. While consumers benefit, the highly contentious public rivalry raises questions about the safety of each airline, the ability of the Mozambican government to regulate competition in the airline industry, and future prospects for air transport privatization. Post has requested an FAA staff visit to Mozambique for June 2005 to assess airline safety and GRM regulatory capacity. End Summary.

Air Corridor

¶2. (SBU) Air Corridor, owned by Mozambican citizens of South Asian origin, opened for business in August 2004 and became the first airline to compete directly with the state-owned airline LAM on its principal domestic routes. Air Corridor early on experienced several in-flight incidents widely reported in the local press (reftel). These consisted of a dangerous approach when Air Corridor and another plane attempted to land simultaneously on the same strip and another in which the company's one Boeing 737-200 sucked a bird into one of its engines, causing a two-day service shutdown. Based on the potential seriousness of the incidents, and with guidance from the Department, the Embassy issued a warden system advisory in December 2004 notifying the American community of our decision not to use Air Corridor for official travel.

¶3. (U) There have been no more safety incidents reported since then. In fact, subsequent discussions with GRM authorities suggest that other airlines and airport maintenance staff may have caused the 2004 incidents (see reftel). In any case, consumers have been happy to take advantage of Air Corridor's low prices, which are 65 to 70 percent below those charged by LAM in 2003-2004. (LAM has responded by cutting its own fares to levels slightly above Air Corridor prices.) For example, a one-way Air Corridor ticket from Maputo to Air Corridor's home city of Nampula now costs only $60, which is only $20 more expensive than the bone-crunching 40-hour bus ride. Air Corridor is starting to see the benefits of its pricing policy; company officials indicated to Emboff that occupancy rates were steadily rising, and averaged nearly 60% in March/April 2005 - up from an estimated 45% in October 2004. The approximately 100 Amcits in and near Nampula have also noticed. Several Nampula-area Amcits recently contacted by the Embassy have told us they have used the airline, found it generally superior to LAM, and have recommended further travel with Air Corridor.

Is This Fair Competition?

¶4. (SBU) It is unclear how Air Corridor and LAM are able to charge such low prices and survive. To a certain extent, each company could justify slashing fares due to the strengthened Mozambican metical, which rose against the dollar from 24,000 mt/$ to 19,000 mt/$ during the latter half of 2004, permitting the companies to purchase fuel much more cheaply. This year, however, the metical has lost nearly all it had gained, causing gas prices to climb again and squeeze profit margins. LAM believes that current airfares are unreasonable and, in various public statements, has charged Air Corridor with "dumping." LAM Managing Director Jose Viegas told Emboff that Air Corridor is pricing tickets well below cost, considering together the costs of general insurance, fuel, fuel insurance, salaries, airport fees, and the $300,000 per month cost of wet leasing a Boeing 737-200 from Phoenix Aviation. He believes Air Corridor provided the GRM with false insurance papers, and really does not carry insurance that properly reflects post-911 premiums and coverage. Another critic, Segundo Alves Gomes, president of the Association of Mozambican Airline Operators, believes the GRM,s agreement to license Air Corridor was illegal because the proper paperwork was not filed.

¶5. (U) (Note: LAM, for its part, dry leases its fleet of three Boeing 737-200s. Two of these are from a US company,

International Aviation Partners, Inc. Viegas said that he is negotiating to lease an additional Boeing 737-200 from this company when the lease on his third airplane ends in October ¶2005. Dry leases, unlike wet leases, do not include payments for crew and maintenance, and generally run $50-65K per month, according to Viegas. End Note.)

¶6. (U) The broadside fired by LAM has started a discussion within the GRM and the industry about what constitutes fair competition. Both LAM and Air Corridor agree the industry needs better regulations, and each has written to the Civil Aviation Institute of Mozambique (IACM) with their requests for an improved legal and institutional structure. In recent conversations with Emboff, Antonio Pinto, director of IACM, lamented the GRM,s lack of relevant laws defining rules of competition in the marketplace and the lack of economic expertise necessary to determine whether "dumping" has taken place. He asked for USG technical assistance in developing an improved regulatory structure, whether from FAA, USAID, or other sources.

Privatization Issues

¶7. (U) The sudden, fierce competition between LAM and Air Corridor has pre-empted the decade-old debate of whether, when, and how LAM should be privatized. LAM, owned 80% by the GRM and 20% by its employees, has long been considered by the GRM to be a strategic company that should not be privatized. International financial institutions, however, have been urging its sale. But with long-standing multi-million dollar debts to Boeing and a 750-employee workforce considered by the World Bank to be more than twice as large as necessary, attractive suitors for LAM have been few and far between. Air Mauritius made the last serious offer for LAM, offering $3.6 million in 1997, which the GRM turned down. Given today's high fuel prices and insurance premiums, compounded by the loss of LAM,s monopoly, well-placed observers in both the World Bank and the airline doubt the GRM could even give LAM away for free today.

¶8. (SBU) While LAM privatization is on hold indefinitely, privatization of airport services apparently is only on hold temporarily. On January 13, 2005, a few weeks before the Chissano government left office, the Council of Ministers approved a 25-year concession of the Maputo airport to Airports Company South Africa (ACSA). ACSA won a competitive bidding process on airport services carried out in 2003. The agreement would have given ACSA 70% stake in airport services, leaving the government with the rest. ACSA, in turn, would have secured a $30 million loan to upgrade Maputo airport. In late March 2005, incoming Minister of Transportation Antonio Munguambe de-authorized the Council of Ministers, concession. (Comment: Post understands that this is a legal maneuver under Mozambican law.) According to LAM and the Ministry, Munguambe decided the concession needed to be re-negotiated, considering that Maputo is the only one of the country's 18 airports that turns an annual profit. Moreover, its revenues have historically been used to finance minimal upgrades at the other airports, something the concession appeared to overlook. Both of the major domestic airlines and several new cabinet ministers, many of whom have just returned to Maputo after stints as governors or high-ranking officials in faraway central and northern provinces, have backed Munguambe's decision. These same sources indicate that the Ministry of Transportation is actively negotiating with ACSA, and they expect a new deal to be struck sometime soon.

FAA Visit

¶9. (SBU) Post will continue the monitor economic and security issues in the Mozambican airline industry, but we do not have the technical expertise to assess a particular airline's safety record. Therefore we have asked the FAA regional representative in Dakar to come to Mozambique to evaluate Air Corridor and LAM, preferably in late June. In the meantime, post has requested from IACM the latest reports from the ICAO and IATA. IATA staff visited Mozambique in April 2005 and made a cursory review of LAM and Air Corridor; Air Corridor hopes for a full inspection by IATA sometime soon as a precursor for gaining membership. ICAO visited Mozambique in late 2004. When post receives the documents requested, we will forward them to FAA-Dakar and the Department.
Dudley